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ACTION TRSE-00

INFO OCT-01 EA-11 ISO-00 NEA-14 IO-14 L-03 H-03 PA-04

PRS-01 USIA-15 SP-03 AID-20 EB-11 NSC-07 RSC-01

CIEP-02 SS-20 STR-08 OMB-01 CEA-02 CIAE-00 COME-00

FRB-02 INR-10 NSAE-00 XMB-07 OPIC-12 LAB-06 SIL-01

DRC-01 /180 W

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R 210908Z JUN 74

FM AMEMBASSY MANILA

TO SECSTATE WASHDC 4587

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USADB

FOR NAC AGENCIES

E.O. 11652: DECLAS 6/30/75

TAGS: EAID,EFIN

SUBJECT: CRITERIA FOR LENDING FROM THE ASIAN DEVELOPMENT FUND

SUMMARY: IN VIEW PENDING CREATION ASIAN DEVELOPMENT FUND (ADF) AND RECENT SOFTENING AND STANDARDIZATION OF SPECIAL FUNDS LOAN TERMS, MANAGEMENT DESIRES ADOPTION OF MORE PRECISE GUIDELINES FOR OPERATIONS OF ADB. BANK PROPOSES TO DIVIDE DEVELOPING MEMBER COUNTRIES (DMC) INTO SUB-GROUPS BASED ON PER CAPITA GNP. CUTOFF LINE FOR GENERAL ELIGIBILITY WILL BE US\$300 IN TERMS OF 1972 GNP. IN ADDITION, BANK WILL ALSO APPLY TEST OF CAPACITY TO REPAY AS WELL AS ABSORPTIVE CAPACITY. PROPOSED GUIDELINES ARE MORE PRECISE THAN EXISTING RULES ADOPTED IN 1972, BUT STILL CONTAIN FLEXIBILITY. USADB GENERALLY SATISFIED WITH PROPOSAL AND RECOMMENDS FAVORABLE ACTION BY NAC.

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1. ADB WORKING PAPER 6-74 ENTITLED "CRITERIA FOR LENDING FROM THE ASIAN DEVELOPMENT FUND" DATED JUNE 20, IS SCHEDULED FOR BOARD CONSIDERATION ON JULY 9.

2. EXISTING GUIDELINES WERE APPROVED BY BOARD IN JULY 1972 TO GUIDE OPERATIONS OF BANK'S MULTIPURPOSE SPECIAL FUNDS, IN VIEW PENDING ACTIVATION OF ASIAN DEVELOPMENT FUND (NOW SCHEDULED ON JUNE 30, 1972) AND RECENT SOFTENING AND STANDARDIZATION OF SPECIAL FUNDS LOAN TERMS (R33-74), MANAGEMENT FEELS ADOPTION OF NEW AND MORE PRECISE GUIDELINES IS DESIRABLE. TERMS AND CONDITIONS FOR LOANS FROM SPECIAL FUNDS WERE SOFTENED AND STANDARDIZED (ON 3/29/74) AS FOLLOWS: ONE PERCENT PER ANNUM SERVICE CHARGED AND 40-YEAR AMORTIZATION PERIOD INCLUDING TEN YEAR GRACE AND REPAYMENT OF PRINCIPAL AT RATE OF TWO PERCENT FOR TEN YEARS AFTER GRACE PERIOD AND AT FOUR PERCENT PER ANNUM FOR REMAINING 20 YEARS. MANAGEMENT ALSO NOTES SOME OF EXISTING GUIDELINES HAVE CHANGED IN THEIR SIGNIFICANCE AND APPLICABILITY TO ACTUAL OPERATIONS DUE TO CHANGED CIRCUMSTANCES IN NUMBER OF DMCS.

3. BASED ON PROVISIONS STIPULATED IN "REGULATIONS OF THE ASIAN DEVELOPMENT FUND", OPERATIONS OF ADF MUST BE GUIDED BY FOLLOWING PRINCIPLES: (A) DUE REGARD MUST BE GIVEN TO ECONOMIC SITUATION OF DMCS, (B) BANK HAS SPECIAL RESPONSIBILITY TO ASSIST IN MEETING NEEDS OF LESS DEVELOPED DMCS, AND (C) EMPHASIS MUST BE PLACED ON PROJECTS AND PROGRAMS OF HIGH DEVELOPMENTAL PRIORITY IN ELIGIBLE DMCS.

4. WORKING PAPER POINTS OUT THAT PROPOSED BASIC GUIDELINE IN DETERMINING ELIGIBILITY FOR LOANS FROM ADF WILL BE ENTIRELY BASED ON COUNTRY CONSIDERATIONS, WHEREAS PRESENT POLICY RECOGNIZES COUNTRY ECONOMIC SITUATION AS MOST IMPORTANT CONSIDERATION. WHILE IT WOULD BE HIGHLY DESIRABLE AND SIMPLE TO HAVE A SINGLE INDICATOR OR FORMULA TO EXPRESS ECONOMIC CONDITION OF DMCS, THIS BEING NOT THE CASE, BANK INTENDS TO EMPLOY SEVERAL INDICATORS, BOTH QUALITATIVE AND QUANTITATIVE, TO REFLECT COUNTRY CONSIDERATIONS.

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5. AS ONE OF BASIC INDICATORS, MANAGEMENT CONSIDERS IT APPROPRIATE FOR BANK TO USE PER CAPITA GNP FIGURE TO GROUP DMCS INTO THOSE ELIGIBLE AND THOSE NOT ELIGIBLE FOR FINANCING FROM ADF. SUGGESTED GENERAL CUTOFF POINT IS US\$300 IN TERMS OF PER CAPITA GNP FOR 1972. MANAGEMENT IS RECOMMENDING A SOMEWHAT LOWER FIGURE THAN THAT OF IDA (I.E., \$375) DUE PRIMARILY CONSTRAINTS ON FUNDS

AVAILABILITY. ELIGIBLE COUNTRIES IN TURN WILL BE DIVIDED INTO THREE SUB-GROUPS AS FOLLOWS: (A) PER CAPITA GNP \$100 OR BELOW: BANGLADESH, INDONESIA, AFGHANISTAN, BURMA, AND NEPAL; (B) PER CAPITA GNP \$101-200: SRI LANKA, LAOS, VIETNAM, KHMER REPUBLIC, PAKISTAN, WESTERN SAMOS, AND TONGA; AND (C) PER CAPITA GNP \$201-300: BRITISH SOLOMON ISLANDS, THAILAND, PHILIPPINES, KOREA, AND PAPUA NEW GUINEA. ON STRICTLY PER CAPITA GNP GROUNDS, SUB-GROUPS (A) AND (B) WOULD BE CONSIDERED DEFINITELY ELIGIBLE WHILE COUNTRIES IN SUB-GROUP (C) WOULD BE TERMED "MARGINALLY ELIGIBLE". COUNTRIES DEFINITELY NOT ELIGIBLE FOR ADF FINANCING WOULD BE MALAYSIA, FIJI, HONG KONG AND SINGAPORE.

6. IN ADDITION TO PER CAPITA GNP FACTOR, DMCS' CAPACITY TO REPAY EXTERNAL DEBT TO BE TAKEN INTO ACCOUNT IN DETERMINING ELIGIBILITY. STRAIGHT DEBT-SERVICE RATIO OR ADJUSTED DEBT-SERVICE RATIO WOULD BE CONSIDERED IN CONTEXT OF STRUCTURE OF ECONOMY OF EACH DMC, ITS GENERAL BALANCE OF PAYMENTS SITUATION AND PROSPECTS, ITS EXISTING STAGE OF DEVELOPMENT, AND GOVT EFFICIENCY AND INSTITUTIONAL CAPABILITIES. THEREFORE, A DMC CONSIDERED AS ELIGIBLE ON PER CAPITA GNP BASIS MIGHT NOT NECESSARILY QUALIFY FOR ADB FINANCING ON GROUNDS OF UNUSUAL CAPACITY TO REPAY DEBT. INDONESIA IS CITED AS ON EXAMPLE OF SUCH DMCS. WORKING PAPER NOTES THAT IF REPAYMENT CAPACITY CONTINUES TO IMPORVE, INDONESIA MAY BE ABLE TO MEET ENTIRE EXTERNAL RESOURCE REQUIREMENTS ON TERMS HARDER THAN HITHERTO.

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FOR NAC AGENCIES

7. WORKING PAPER FURTHER NOTES THAT FINANCING FROM ADB WOULD NOT BE PROPORTIONAL TO DEGREE OF ELIGIBILITY INDICATED BY PER CAPITA GNP AND JUDGMENT ON CAPACITY TO REPAY DEBT. AVAILABILITY OF SOUND AND VIABLE PROJECTS WOULD BE STILL ANOTHER FACTOR IN ELIGIBILITY DETERMINATION. ABSORPTIVE CAPACITY INDICATED BY DMCS TECHNICAL, ADMINISTRATIVE, AND INSTITUTIONAL CAPABILITIES TO PREPARE AND IMPLEMENT PROJECTS WOULD BE CAREFULLY EVALUATED TO DETERMINE EXTENT OF BANK ASSISTANCE THROUGH ADB.

8. SO-CALLED "Marginally Eligible" DMCS (Korea, Philippines and Thailand) have received only occasionally limited amounts from special funds in relation to their total borrowings from bank. In future, management points out, any ADF financing to these DMCS would depend on their economic circumstances and on availability of resources and, in any case, would not be more than limited amount

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OF TOTAL FINANCING PROVIDED TO THEM BY BANK. (In this regard, working paper indicates World Bank group recently decided not to make IDA funds available to Thailand and similar decision may be in offering for some other borderline countries.) Papua New Guinea and British Solomon Islands (sub-group C), however, would be given special consideration by bank due to fact that their per capita GNP is highly distorted because of predominance of small but high income non-indigenous sector.

9. Although not related to criteria, working paper proposes to permit blend of ordinary capital and concessional resources on both country and project basis.

10. Proposed guidelines are more precise than existing rules in that DMCS will actually be classified by per capita GNP into categories of eligible and non-eligible. But as factors such as debt repayment capacity and absorptive capacity must also be considered. USADB intends to explore exactly how these two additional

TESTS WOULD BE APPLIED IN ACTUAL OPERATIONS. USADB ALSO
INTENDS TO REMIND BANK OF ADMINISTRATIVE DIFFICULTIES
ASSOCIATED WITH PROJECT BLENDING. USADB AGREES THAT
ADOPTION OF NEW GUIDELINES IS TIMELY AND IS SATISFIED
GENERALLY WITH PRELIMINARY WORKING PAPER.
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